



# Duties of supervisory board and powers of activist shareholders revisited

DUTCH SUPREME COURT'S DECISION ON ASMI

In its recent decision on ASMI the Supreme Court of the Netherlands confirmed that the strategy of a company is part of the management board's competency. In principle, the management board is not required to involve shareholders before its decision making in matters of strategy or to enter into discussions with activist shareholders that disagree with the management board's position. Furthermore, the supervisory board is not obliged to mediate in conflicts between the management board and the shareholders, and the management and supervisory board are free to appoint (strategic) advisers, even if these advisers play a crucial role with respect to the policies of the company. This briefing explains these and other findings and summarises their implications for Dutch businesses.

## Introduction

On 9 July 2010 the Supreme Court of the Netherlands rendered an important decision that further defines the corporate governance of a Dutch listed company and the responsibilities of its management and supervisory boards against the backdrop of actions of activist minority shareholders. In its decision on ASM International (ASMI) the Supreme Court annulled the earlier decision of the Enterprise Chamber of the Amsterdam Court of Appeal in an inquiry proceeding initiated by, among others, the two activist minority shareholders Hermes and Fursa. This briefing outlines the main features of the Supreme Court's decision.

## Strategy of a company is part of the management board's competency

According to the Enterprise Chamber in its decision of 5 August 2009, ASM International (ASMI) failed to properly address problems related to the company's (corporate) strategy – or, at least, had tried to solve these problems within a closed group of persons, comprising the (former) chief executive officer, the supervisory board members and its majority shareholder. In doing so, the Enterprise Chamber decided, ASMI had positioned itself in a reticent and defensive way towards the other shareholders and used its outdated corporate governance structure for that purpose. External investors, such as Hermes and Fursa, had almost no influence on ASMI's strategy and there was no way for them to effectively hold ASMI's management or supervisory

board accountable on strategy issues, according to the Enterprise Chamber.

Confirming its earlier decision in the 2007 ABN AMRO inquiry proceeding, the Supreme Court finds that a company's strategy is, in principle, part of the management board's competency. It is up to the management board's own discretion – under the supervision of the supervisory board – to decide whether and to what extent it wants to discuss the company's strategy with its shareholders. Except as provided otherwise by law or the company's articles of association, the management board is not required to involve shareholders before its decision making in matters that are part of the management board's competency, although the management board is accountable to the general meeting for the policies pursued.

The fact that external investors – such as Hermes and Fursa – disagree with the position of the management board and the supervisory board does not in itself, according to the Supreme Court, lead to the conclusion that the management board is required to enter into discussions with those investors, and the management board by not doing so does not demonstrate a defensive or reticent attitude. However, the Supreme Court also found that the Enterprise Chamber's reasoning in this respect was 'less comprehensible' where there had been evidence that the management board actually had held discussions with Hermes and Fursa and had indicated that it was willing to bring ASMI's outdated corporate governance structure in line with the Dutch Corporate Governance Code.

### **Inquiry proceeding**

Under Dutch law, the Enterprise Chamber of the Amsterdam Court of Appeals has the authority to order an inquiry into the policies and affairs of a Dutch company at the request of certain interested parties, in the case of possible mismanagement.

The term ‘mismanagement’ (*wanbeleid*) is not defined by law. Mismanagement is not limited to the management by the managing directors but can relate to acts by supervisory directors, shareholders or others within the company, as well. Mismanagement refers to a condition of a company. It includes the inadequate functioning of the company as a legal entity. The Enterprise Chamber has held that ‘to act contrary to elementary principles of running an enterprise in a sound manner’ constitutes mismanagement.

If there are well-founded reasons to question whether a Dutch company pursues proper policies, the Enterprise Chamber may order an inquiry and appoint investigators to carry it out. The Enterprise Chamber will have to determine on the basis of the facts as set out in the investigators’ report whether mismanagement has taken place.

There is the possibility of appeal to the Supreme Court of the Netherlands against the Enterprise Chamber’s decision. The Supreme Court will not conduct another full review of the case, but will merely assess whether the Enterprise Chamber has correctly applied Dutch law. Its ASMI decision is the result of an appeal against the Enterprise Chamber’s decision to order an inquiry into the policies and affairs of ASMI.

### **Mediating role for the supervisory board**

In its judgment the Enterprise Chamber ruled that the supervisory board of ASMI failed to take responsibility for bringing the management board closer to Hermes and Fursa.

According to statutory law, the supervisory board is responsible for supervising the management board and the company’s general affairs and needs to give the management board its advice. However, according to the Supreme Court, this does not imply that the supervisory board is obliged to mediate in conflicts between the management board and the shareholders or certain groups of shareholders and there is no accountability of the supervisory board to the shareholders in this respect.

Best practice rule III.1.6(f) of the Dutch Corporate Governance Code, which provides that supervision of the management board by the supervisory board of a listed company also includes supervision over the relationship between the company and its shareholders, and article 2:8 of the Dutch Civil Code, under which a company must act in accordance with the principles of reasonableness and fairness towards the various

parties involved in its governance, do not lead to a different conclusion. If the shareholders ask the supervisory board to mediate or take any other action, the supervisory board has to respond adequately to the request in accordance with what it sees as its duties and responsibilities. According to the Supreme Court, a requirement for the supervisory board to mediate (*pro-actively*) would be inconsistent with its discretionary powers in carrying out its duties. The supervisory board must have the discretion on a case-by-case basis to balance whether it is desirable and in the company’s interests to enter into direct contact with shareholders or to mediate between shareholders and the management board.

Furthermore, the Supreme Court ruled that the management board and the supervisory board are free to appoint (strategic) advisers, even if these advisers play a crucial role with respect to the policies (including the strategy) of the company. This does not prevent the general meeting of shareholders from exercising its statutory rights and competences, because the general meeting may call the corporate body that appointed the relevant adviser to account with respect to the choice of the adviser or on the manner in which the adviser carried out its duties and, furthermore, may challenge the management board and the supervisory board over the company’s policies.

### **Role of the ASMI anti-takeover foundation**

ASMI had an anti-takeover instrument in place in the form of a foundation (*Stichting Continuïteit*) that had an option to call preference shares that, when exercised, would give the foundation up to almost 29 per cent of the voting rights in the general meeting of shareholders of ASMI. The foundation (with a board independent from the board of ASMI) actually exercised that option, which thwarted the activist shareholders’ efforts to replace the management board of ASMI. The Enterprise Chamber ruled that by exercising the call option the foundation had contributed to the policies of ASMI and could, therefore, be considered to co-determine ASMI’s policies, so the exercise of the call option could be part of the investigation.

The Supreme Court, however, found that the exercise of the call option did not constitute a policy of ASMI itself

and consequently the foundation could not be seen as a co-policymaker of ASMI.

## Conclusion

In this decision the Supreme Court seems to put certain limits on the inquiry proceeding as a means for activist shareholders to force their way on a Dutch listed company. We expect that the standards set out by the Supreme Court in this decision will play a role in any future disputes involving a Dutch (listed) company, its management board, supervisory board and any activist minority shareholders.

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